

'06

State of Utah

Comprehensive Annual Financial Report



For the Fiscal Year Ended **June 30, 2006**



State Of Utah
COMPREHENSIVE ANNUAL FINANCIAL REPORT
For The Fiscal Year Ended June 30, 2006

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Special appreciation is given to all of the budget and accounting officers throughout the State whose extra time and effort made this report possible.



State of Utah
COMPREHENSIVE ANNUAL FINANCIAL REPORT

For the Fiscal Year Ended June 30, 2006

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INTRODUCTION

The following is a discussion and analysis of the State of Utah's financial performance and position, providing an overview of the State's activities for the fiscal year ended June 30, 2006. Please read it in conjunction with the transmittal letter in the Introductory Section of this report and with the State's financial statements that follow this section.

HIGHLIGHTS

Government-wide

- The State's total net assets increased \$1.864 billion or 15.3 percent over the prior year. Net assets of governmental activities increased \$1.549 billion or 14.9 percent due to an improving economy and active resource management. Net assets of business-type activities also grew significantly, increasing by \$315.2 million or 18.0 percent, primarily due to revenues from employers' unemployment premiums exceeding benefit payments for the second consecutive year.

Fund Level

- Combined tax revenues were 10.2 percent higher in the General Fund and 25.2 percent higher in the Uniform School Fund than the prior year as Utah's economy showed continued signs of improvement. The State's economic slowdown in 2002 and 2003 and subsequent improvement in fiscal years 2004 through 2006 is similar to the trend of the national economy.
- The General Fund and Uniform School Fund ended the fiscal year with "surplus" from unreserved and undesignated sources of \$85.1 million and \$223.3 million, respectively. By law, \$21.9 million of the surplus in the General Fund was transferred to the General Fund Budget Reserve Account ("Rainy Day Fund"), and \$56.6 million of the surplus in the Uniform School Fund was transferred to the Education Budget Reserve Account.

Long-term Debt

- The State's long-term bonded debt increased a net \$433.4 million or 12.5 percent. Revenue bonds were issued to fund capital facility construction, and for purchasing student loans in the Student Assistance Programs. No new general obligation bonds were issued.

OVERVIEW OF THE FINANCIAL STATEMENTS

This report includes the State's Basic Financial Statements, Required Supplementary Information, and Supplementary Information. The Basic Financial Statements include three components: government-wide financial statements, fund financial statements, and notes to the financial statements.

Government-wide Statements – Reporting the State as a Whole

The Statement of Net Assets and the Statement of Activities beginning on page 27 together comprise the *government-wide financial statements*. These statements provide a broad overview with a long-term focus of the State's finances as a whole and are prepared using the *full-accrual* basis of accounting, similar to private-sector companies. This means all revenues and expenses are recognized regardless of when cash is received or spent, and all assets and liabilities, including capital assets and long-term debt, are reported at the entity level.

The government-wide statements report the State's *net assets* – the difference between total assets and total liabilities – and how they have changed from the prior year. Over time, increases and decreases in net assets measure whether the State's overall financial condition is getting better or worse. In evaluating the State's overall condition, however, additional non-financial factors should be considered such as the State's economic outlook, changes in its demographics, and the condition of its capital assets and infrastructure. The government-wide statements report three activities:

Governmental Activities – Most of the State's basic services fall under this activity including education, transportation, public safety, courts, corrections, health, and human services. Taxes and federal grants are the major funding sources for these programs.

Business-type Activities – The State operates certain activities much like private-sector companies by charging fees to customers to cover all or most of the costs of providing the goods and services. Student loans, unemployment compensation, water project loan programs, and liquor sales are examples of business-type activities.

Component Units – A number of entities are legally separate from the State, yet the State remains financially accountable for them. Colleges and Universities, Utah Housing Corporation, and Utah State Fair Corporation are examples of component units.

Fund Financial Statements – Reporting the State's Most Significant Funds

The fund financial statements beginning on page 32 provide detailed information about individual major funds, not the State as a whole. A fund is a group of related accounts that the State uses to keep track of specific resources that are segregated for a specific purpose. Some funds are required by law to exist, while others are established internally to maintain control over a particular activity. All of the State's funds are divided into three types, each of which uses a different accounting approach.

Governmental Funds – Most of the State's basic services are accounted for in governmental funds and are essentially the same functions reported as *governmental activities* in the government-wide statements. Governmental funds use the *modified accrual* basis of accounting, which measures the flow of current financial resources that can be converted to cash and the balances left at yearend that are available for future spending. This *short-term* view of the State's financial position helps determine whether the State has sufficient resources to cover expenditures for its basic services in the near future.

Proprietary Funds – Proprietary funds include enterprise funds and internal service funds and account for state activities that are operated much like private-sector companies. Like the government-wide statements, proprietary fund statements are presented using the *full-accrual* basis of accounting. Activities whose customers are mostly outside of state government (e.g., water project loans to local governments) are accounted for in *enterprise funds* and are the same functions reported as *business-type activities*. Thus, the *enterprise fund* financial statements reinforce the information reported for *business-type* activities in the government-wide statements, but provide more detail and additional information, such as cash flows. Activities whose customers are mostly other state agencies (e.g., motor pool) are accounted for in *internal service funds*. The internal service fund activities are consolidated with the governmental activities in the government-wide statements because those services predominantly benefit governmental rather than business-type activities.

Fiduciary Funds – Fiduciary funds account for assets that, because of trust relationships, can be used only for trust beneficiaries. The State is responsible for ensuring these assets are used for their intended purposes. Fiduciary funds use *full-accrual* accounting but are *not* included in the government-wide statements because their assets are not available to finance the State's own programs.

Reconciliation between Government-wide and Fund Statements

The financial statements include schedules on pages 34 and 38 that reconcile and explain the differences between the amounts reported for *governmental activities* on the government-wide statements (full-accrual accounting, long-term focus) with amounts reported on the *governmental* fund statements (modified accrual accounting, short-term focus). Following are some of the major differences between the two statements:

- Capital assets and long-term debt are included on the government-wide statements but are not reported on the governmental fund statements.
- Capital outlay spending results in capital assets on the government-wide statements but are expenditures on the governmental fund statements.
- Bond proceeds result in liabilities on the government-wide statements but are other financing sources on the governmental fund statements.
- Certain tax revenues that are earned but not yet available are reported as revenue on the government-wide statements but are deferred revenue on the governmental fund statements.

Notes to the Financial Statements

The notes beginning on page 58 provide additional schedules and information that are essential to a complete understanding of the financial statements. The notes apply to both the government-wide financial statements and the fund financial statements.

Required Supplementary Information (RSI)

Following the Basic Financial Statements are budgetary comparison schedules for major funds with legally adopted budgets and condition assessment data related to infrastructure. RSI further supports the information in the basic financial statements.

Supplementary Information

Supplementary Information includes combining statements for the State's nonmajor governmental, nonmajor proprietary and fiduciary funds and for nonmajor discretely presented component units. This section also includes schedules which compare budgeted expenditures to actual results at the legal level of control, which is generally the line item level of the *Appropriation Acts*.

FINANCIAL ANALYSIS OF THE STATE AS A WHOLE

Net Assets

The State's total net assets increased \$1.864 billion or 15.3 percent in fiscal year 2006. In comparison, net assets in the prior year increased \$1.012 billion or 9.1 percent. This increase in net assets resulted from an improving economy and the active management of state resources. Approximately \$526.1 million of the increase was in net capital assets as the State's investment in highways and buildings exceeded depreciation and net additional debt to finance projects. Total restricted net assets increased \$1.072 billion or 43.8 percent over the prior year. The \$860.7 million increase in restricted net assets of governmental activities was primarily due to an increase of \$709.7 million in expendable net assets for public education as a result of increased individual income and corporate tax revenues. Also, nonexpendable net assets for public education increased \$156.8 million as a result of an increase in net earnings in the permanent Trust Lands Fund. Restricted net assets increased in business-type activities by \$211.6 million primarily due to unemployment compensation revenues exceeding related claims by \$174.9 million. The increase of \$166.0 million in unrestricted net assets of governmental activities was primarily due to an increase in the unrestricted carry-forward balances in the General Fund of \$202.7 million less decreases in carry-forward balances of other government funds. The increase of \$100.0 million in unrestricted net assets of business-type activities was the result of normal operations and is primarily due to the State adding additional capital to the loan funds from mineral lease revenues and sales taxes. Net assets of business-type activities generally can be used only to finance the business-type activities' ongoing operations.

State of Utah
Net Assets as of June 30
(Expressed in Thousands)

	Governmental Activities		Business-type Activities		Total Primary Government	
	2006	2005	2006	2005	2006	2005
Current and Other Assets	\$ 4,356,335	\$ 3,358,120	\$ 4,294,237	\$ 3,375,986	\$ 8,650,572	\$ 6,734,106
Capital Assets	10,247,267	9,860,641	66,974	62,154	10,314,241	9,922,795
Total Assets	14,603,602	13,218,761	4,361,211	3,438,140	18,964,813	16,656,901
Current and Other Liabilities	692,891	699,180	47,057	39,972	739,948	739,152
Long-term Liabilities	1,955,484	2,113,602	2,249,277	1,648,535	4,204,761	3,762,137
Total Liabilities	2,648,375	2,812,782	2,296,334	1,688,507	4,944,709	4,501,289
Net Assets:						
Invested in Capital Assets,						
Net of Related Debt	8,719,751	8,197,279	32,068	28,419	8,751,819	8,225,698
Restricted	2,379,269	1,518,523	1,139,691	928,115	3,518,960	2,446,638
Unrestricted	856,207	690,177	893,118	793,099	1,749,325	1,483,276
Total Net Assets	\$ 11,955,227	\$ 10,405,979	\$ 2,064,877	\$ 1,749,633	\$ 14,020,104	\$ 12,155,612
Percent change in total net assets from prior year	14.9 %		18.0 %		15.3 %	

The largest component of the State's net assets, 62.4 percent, reflects investments in capital assets (e.g., land, buildings, equipment, roads, and other infrastructure) less the outstanding debt issued to finance those assets. As capital assets, these resources are not available for future spending, nor can they be readily liquidated to pay off their related liabilities. Resources needed to repay capital-related debt must be provided from other sources.

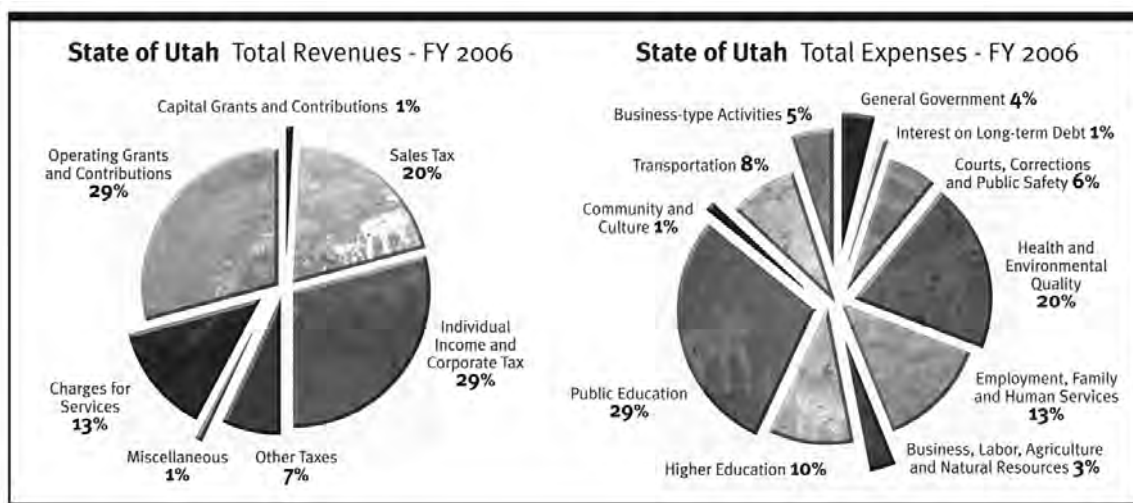
Restricted net assets comprise 25.1 percent of total net assets and are subject to constitutional, legal, or external constraints on how they can be used. Net assets that are restricted by the *Constitution of Utah* include income and corporate taxes that can be used only for public and higher education costs and for motor fuel taxes that can be used only for transportation expenses.

The remaining balance of unrestricted net assets may be used to meet the State's ongoing obligations, though certain laws and internally imposed designations of resources further limit the purposes for which many of those net assets may be used.

The schedule and charts that follow summarize the State's total revenues, expenses, and changes in net assets for fiscal year 2006.

State of Utah
Changes in Net Assets
for the Fiscal Year Ended June 30
(Expressed in Thousands)

	Governmental Activities		Business-type Activities		Total Primary Government		Total Percentage Change
	2006	2005	2006	2005	2006	2005	2005 to 2006
Revenues							
General Revenues:							
Taxes	\$ 5,470,916	\$ 4,519,789	\$ 14,875	\$ 14,874	\$ 5,485,791	\$ 4,534,663	21.0 %
Other General Revenues	124,939	65,481	308	4,070	125,247	69,551	80.1 %
Program Revenues:							
Charges for Services	705,095	615,844	589,104	507,583	1,294,199	1,123,427	15.2 %
Operating Grants and Contributions	2,744,231	2,436,116	109,140	65,173	2,853,371	2,501,289	14.1 %
Capital Grants and Contributions	100,519	124,836	—	—	100,519	124,836	(19.5)%
Total Revenues	9,145,700	7,762,066	713,427	591,700	9,859,127	8,353,766	18.0 %
Expenses							
General Government	289,749	240,091	—	—	289,749	240,091	20.7 %
Human Services and Youth Corrections	595,337	573,154	—	—	595,337	573,154	3.9 %
Corrections, Adult	208,922	195,716	—	—	208,922	195,716	6.7 %
Public Safety	182,042	162,922	—	—	182,042	162,922	11.7 %
Courts	109,180	98,319	—	—	109,180	98,319	11.0 %
Health and Environmental Quality	1,635,544	1,461,016	—	—	1,635,544	1,461,016	11.9 %
Higher Education	810,228	694,732	—	—	810,228	694,732	16.6 %
Employment and Family Services	405,845	409,334	—	—	405,845	409,334	(0.9)%
Natural Resources	133,441	121,714	—	—	133,441	121,714	9.6 %
Community and Culture	84,843	86,065	—	—	84,843	86,065	(1.4)%
Business, Labor, and Agriculture	90,573	84,992	—	—	90,573	84,992	6.6 %
Public Education	2,321,139	2,169,071	—	—	2,321,139	2,169,071	7.0 %
Transportation	640,251	579,914	—	—	640,251	579,914	10.4 %
Interest on Long-term Debt	70,345	76,382	—	—	70,345	76,382	(7.9)%
Student Assistance Programs	—	—	152,895	95,495	152,895	95,495	60.1 %
Unemployment Compensation	—	—	102,476	142,632	102,476	142,632	(28.2)%
Water Loan Programs	—	—	6,560	8,648	6,560	8,648	(24.1)%
Other Business-type Activities	—	—	155,265	141,374	155,265	141,374	9.8 %
Total Expenses	7,577,439	6,953,422	417,196	388,149	7,994,635	7,341,571	8.9 %
Excess Before Transfers	1,568,261	808,644	296,231	203,551	1,864,492	1,012,195	
Transfers	(19,013)	9,437	19,013	(9,437)	—	—	
Change in Net Assets	1,549,248	818,081	315,244	194,114	1,864,492	1,012,195	
Net Assets – Beginning as Adjusted	10,405,979	9,587,898	1,749,633	1,555,519	12,155,612	11,143,417	
Net Assets – Ending	\$ 11,955,227	\$ 10,405,979	\$ 2,064,877	\$ 1,749,633	\$ 14,020,104	\$ 12,155,612	15.3 %



Changes in Net Assets

This year the State received 55.6 percent of its revenues from state taxes and 30.0 percent of its revenues from grants and contributions, mostly from federal sources. In the prior year, state taxes accounted for 54.3 percent and grants and contributions were 31.4 percent of total revenues. Charges for goods and services such as licenses, permits, liquor sales, state parks, and court fees, combined with other miscellaneous collections, comprised 14.4 percent of total revenues in fiscal year 2006, compared with 14.3 percent in fiscal year 2005.

Governmental Activities

The State's total governmental revenues from all sources increased \$1.384 billion or 17.8 percent. Tax revenues increased \$951.1 million or 21.0 percent. This increase in taxes reflects a continued improvement in economic conditions and is similar to the increase at the fund level. However, due to differences in measurement focus, timing of collections, and lack of historical accrued tax information, the increase at the government-wide level should not be used to predict future increases at the fund statement or budget level. With the exception of higher education, other significant changes in governmental activities' revenues and expenses mirror the changes in the General Fund at the fund level. For further discussion of these changes, see the section entitled "General Fund" on page 19. For fiscal year 2006, higher education expenses increased by \$115.5 million compared to the prior year, due in part to an increase of \$72.9 million spent for building projects completed for colleges and universities. An increase in general state support for higher education accounted for the balance of the increase.

The following table shows to what extent the State's governmental activities relied on taxes and other general revenues to cover all of their costs. For fiscal year 2006, state taxes and other general revenues covered 53.2 percent of expenses. The remaining \$3.550 billion or 46.8 percent of the total expenses were generated through charges for services and grants. As discussed in the "General Fund" section on page 19, federal mineral lease revenues increased significantly in fiscal year 2006. This increase was the largest single factor that caused Program Revenues to exceed Program Expenses by \$41.8 million in the general government function.

State of Utah
Net Cost of Governmental Activities
for the Fiscal Year Ended June 30
(Expressed in Thousands)

	Program Expenses 2006	Less Program Revenues 2006	Net Program Costs		Program Revenues as a Percentage of Program Expenses	
			2006	2005	2006	2005
General Government	\$ 289,749	\$ (331,515)	\$ (41,766)	\$ 28,977	114.4 %	87.9 %
Human Services and Youth Corrections	595,337	(286,594)	308,743	277,765	48.1	51.5 %
Corrections, Adult	208,922	(5,007)	203,915	192,762	2.4	1.5 %
Public Safety	182,042	(102,033)	80,009	65,082	56.0	60.1 %
Courts	109,180	(47,934)	61,246	51,199	43.9	47.9 %
Health and Environmental Quality	1,635,544	(1,265,565)	369,979	317,708	77.4	78.3 %
Higher Education	810,228	(1,536)	808,692	693,106	0.2	0.2 %
Employment and Family Services	405,845	(353,168)	52,677	48,960	87.0	88.0 %
Natural Resources	133,441	(86,037)	47,404	46,642	64.5	61.7 %
Community and Culture	84,843	(40,568)	44,275	42,592	47.8	50.5 %
Business, Labor, and Agriculture	90,573	(73,074)	17,499	16,654	80.7	80.4 %
Public Education	2,321,139	(506,957)	1,814,182	1,722,677	21.8	20.6 %
Transportation	640,251	(449,857)	190,394	196,120	70.3	66.2 %
Interest on Long-term Debt	70,345	—	70,345	76,382		
Total Governmental Activities	\$ 7,577,439	\$ (3,549,845)	\$ 4,027,594	\$ 3,776,626	46.8 %	45.7 %

Business-type Activities

Operating revenues from the State's business-type activities increased \$121.7 million or 20.6 percent from the prior year. This increase is due, in part, to a \$47.6 million increase in revenues in the Student Assistance Programs, as a result of higher interest rates on student loans and an increase in revenues from federal reinsurance. Revenues in the Unemployment Compensation Fund increased \$31.3 million, as higher claims in recent years resulted in increased employer taxes. Liquor sales increased by \$20.2 million, primarily due to higher sales volume. Investment income increased \$15.9 million due to rising interest rates. Total operating expenses for the State's business-type activities increased \$29.0 million, or 7.5 percent. The increase was largely due to claims expenses increasing \$22.5 million in the Student Assistance Programs, as payments to lenders increased for guaranteed claims due to more defaults by borrowers.

All of the State's business-type activities operate from program revenues, except for the Water Loan Programs and the Agriculture Loan Fund that by law receive dedicated sales taxes and the Community Impact Loan Fund that receives federal mineral lease revenues to provide additional capital for loans. Accounting standards require unemployment taxes that are collected from employers and deposited in the Unemployment Compensation Fund be reported as charges for services rather than taxes. Therefore, taxes in the business-type activities are comprised entirely of sales taxes in the water and agriculture loan programs.

FINANCIAL ANALYSIS OF THE STATE'S GOVERNMENTAL FUNDS

Fund Balances

At June 30, 2006, the State's governmental funds reported combined ending fund balances of \$3.173 billion. Of this amount, \$1.587 billion or 50.0 percent is reserved for specific programs by state law, by external constraints, or by contractual obligations. Unspent bond proceeds, balances of restricted accounts, and agencies' nonlapsing balances are included in reserved fund balance. An additional \$1.199 billion or 37.8 percent of total fund balances has been designated through internally imposed limitations on uses of certain funds. Note 11 on page 95 provides more details about reserved and designated fund balances at June 30, 2006. The remaining \$386.9 million or 12.2 percent of fund balance is available for appropriation for the general purposes of the funds.

State of Utah Governmental Fund Balances as of June 30, 2006 (Expressed in Thousands)

	General Fund	Uniform School Fund	Transportation Fund	Transportation Investment Fund	Trust Lands Fund	Nonmajor Funds	Total
Reserved	\$ 300,497	\$ 66,474	\$ 44,961	\$ 143,490	\$ 751,024	\$ 280,634	\$ 1,587,080
Unreserved Designated	483,510	652,613	48,107	672	—	14,432	1,199,334
Unreserved Undesignated	85,129	223,302	116,817	—	—	(38,374)	386,874
Total	\$ 869,136	\$ 942,389	\$ 209,885	\$ 144,162	\$ 751,024	\$ 256,692	\$ 3,173,288
Percent change from prior year	32.90 %	131.83 %	1.86 %	(21.84)%	26.38 %	(22.07)%	33.63 %

General Fund

During fiscal year 2006, the General Fund's total fund balance increased \$215.2 million or 32.9 percent. This increase was due in large part to sales tax revenues coming in \$62.3 million greater than budgeted and to \$155.5 million being set aside in the budget and designated by the Legislature for fiscal year 2007 appropriations. In contrast, in the prior year, the Legislature designated only \$74.6 million for the next year's appropriations. The General Fund ended fiscal year 2006 with a "surplus" from unreserved and undesignated sources of \$108.5 million. State law normally requires 25 percent of the "surplus" to be transferred to the General Fund Budget Reserve Account ("Rainy Day Fund"). However, state law limits the combined totals of the General Fund Budget Reserve Account and the Education Budget Reserve Account to 6 percent of combined appropriations. As a result, \$21.9 million, or 20.2 percent was transferred to the General Fund Budget Reserve Account and included in designated fund balance. An additional \$1.4 million was carried forward by law for other purposes as designated for specific appropriation in 2007. The General Fund ended the year with \$85.1 million in unreserved/undesignated fund balance. Miscellaneous changes resulting from other designated and reserved sources account for the remaining change in fund balance. The General Fund Budget Reserve Account ended fiscal year 2006 with a balance of \$131.6 million.

Total General Fund revenues increased \$416.4 million or 10.0 percent from the prior year. Total tax collections increased \$193.1 million or 10.2 percent. The major positive changes in tax revenues were in sales tax, which increased \$156.6 million or 9.4 percent as Utah's economy continues to improve; and in oil, gas, and mining severance tax, which increased \$23.6 million or 36.4 percent. Federal funding was the largest single factor in increasing non-tax revenues for the fiscal year, as federal mineral lease revenues increased \$74.1 million or 89.7 percent, driven by higher oil prices; and federal contracts and grants climbed \$83.0 million or 4.7 percent from the prior year, driven by demand for services and higher costs.

Total General Fund expenditures increased by \$316.8 million or 7.9 percent. The increase was due in part to a 2.5 percent cost-of-living adjustment provided for state employees and increased costs for employee health and dental benefits of 11.8 and 6.0 percent, respectively. Additional market comparability wage adjustments were also provided to approximately 14,000 state employees. The balance of the increase in expenditures is evidence of a continued high demand for government services. The following areas were impacted most:

- *Health and Environmental Quality* – Total expenditures in this category jumped \$173.6 million, primarily due to increased Medicaid program costs resulting from increased caseloads and inflationary increases for Medicaid provider rates.
- *Higher Education* – Total expenditures in this category were up \$44.2 million, primarily due to additional state appropriations for employee health and dental increases, salary increases, and increases in expenditures for operations and maintenance of existing and new buildings.

In addition to the functions, for fiscal year 2006 the State's economic development function was moved from the Department of Community and Economic Development to the newly created Governor's Office of Economic Development, per HB 318, *Community and Economic Development Restructuring*, 2005 General Session. This change resulted in a shift of expenditures to the general government function of \$25.5 million in fiscal year 2006.

Budgetary Highlights – General Fund

The Legislature adopted the initial fiscal year 2006 budget during the 2005 General Session. The original General Fund budget at the start of fiscal year 2006, excluding department-specific revenue sources such as federal grants, departmental collections, and including miscellaneous transfers, was 6.1 percent higher than the final fiscal year 2005 budget. The Legislature also had to address critical and mandated program increases, such as providing the State's matching share of projected increases in caseloads and inflationary increases for the Medicaid program. Other increases included funding for higher education and increases in employee salaries and benefits.

The budget was again addressed during the 2006 General Session of the Legislature (January to March 2006). General revenue estimates had increased \$186.7 million over those adopted in the 2005 General Session primarily due to increased revenue estimates of sales and use tax. Increased revenue estimates allowed the Legislature to designate \$155.5 million of expected excess revenue for fiscal year 2007 appropriations.

Final budgets of department-specific revenue sources increased over original budgets and actual department-specific revenues increased over final budgets mostly due to an increase in federal mineral lease revenues. Final budgets for many of the departmental-specific revenue sources and related expenditures such as federal grants, departmental collections, and miscellaneous revenues, are generally revised based on actual collections. The difference between final budgeted expenditures and actual expenditures is primarily due to nonlapsing and unspent restricted funds that will be carried forward to the next year. However, \$1.7 million of unspent budgeted dollars were lapsed back to the General Fund by agencies.

Uniform School Fund

The Uniform School Fund's fund balance increased \$535.9 million or 131.8 percent from the prior year. Corporate tax receipts increased \$170.3 million or 81.4 percent compared to the prior year, individual income tax receipts increased \$377.8 million or 19.4 percent, and federal funding increased by \$27.1 million or 7.9 percent. Expenditures for public education increased by \$154.0 million or 7.1 percent, as the Legislature increased the budget for enrollment growth and for increased costs related to employee salary and benefit increases. The Uniform School Fund ended the year with a "surplus" from unreserved and undesignated sources of \$279.9 million. State law normally requires 25 percent of the "surplus" to be transferred to the Education Budget Reserve Account. However, state law limits the combined totals of the General Fund Budget Reserve Account and the Education Budget Reserve Account to 6 percent of combined appropriations. As a result, \$56.6 million or 20.2 percent was transferred to the Education Budget Reserve Account, resulting in a final unreserved and undesignated fund balance of \$223.3 million. Established by the Legislature in 2003, the Education Budget Reserve Account ended fiscal year 2006 with a balance of \$123.4 million.

Transportation Fund

The fund balance of the Transportation Fund increased \$3.8 million or 1.9 percent from the prior year. Revenues increased by \$109.2 million or 14.9 percent, primarily due to a \$55.4 million increase in federal contracts and grants and a \$23.9 million increase in charges for services. Expenditures increased by 108.8 million or 15.8 percent as a result of increased spending on federal participating highway projects.

Authorized federal funding for highway construction remains relatively stable from year to year. However, the spending of state and federal revenue reflects the timing of highway construction projects, which is impacted by a variety of circumstances such as environmental studies or weather. Also, the Department of Transportation has discretion on allocating federal funds among projects, which impacts the amount of federal revenue reported in the Transportation Fund and Transportation Investment Fund.

Transportation Investment Fund

The fund balance of the Transportation Investment Fund decreased by \$40.3 million or 21.8 percent from the prior year. Revenues in the fund increased \$33.7 million or 54.4 percent, mostly due to an increase in sales and use taxes of \$60.3 million as a result of

House Bill 1008, *Transportation Investment Act*, of the 2005 First Special Session. This bill earmarked an additional \$59.6 million from sales and use tax revenue annually for Centennial Highway projects accounted for within this fund. The increase in tax revenues was offset by a decrease in federal revenues of \$27.3 million or 83.5 percent. Expenditures in the fund increased by \$34.9 million or 24.7 percent, primarily in construction expenditures for the projects specific to this fund.

Trust Lands Fund

The fund balance of the permanent Trust Lands Fund increased by \$156.8 million or 26.4 percent due to revenues generated from land use, sales of trust lands, and investment income. The permanent fund also generated \$18.1 of cash investment earnings for the Uniform School Fund that is earmarked for distribution to local school districts. The principal in the fund is held in perpetuity with earnings restricted primarily to support public education.

FINANCIAL ANALYSIS OF THE STATE'S PROPRIETARY FUNDS

Student Assistance Programs

The Student Assistance Programs finished the year with an increase in net assets of \$20.2 million or 8.2 percent. Growth of the student loan portfolio and higher student loan interest rates accounted for most of the increase. As a result, loans receivable increased \$298.6 million or 20.5 percent over last year. Of total net assets of \$265.2 million, \$178.5 million is restricted for use within the Student Assistance Programs by bond covenants or by federal law.

Unemployment Compensation Fund

The State's unemployment rate decreased compared to the rate one year ago. The improving employment situation resulted in a \$40.2 million or 28.2 percent decrease in benefit payments from the prior year. For the second consecutive year, employer taxes and other revenues exceeded benefit payments. Assets were sufficient to handle the demand for benefits, and net assets increased \$174.9 million or 34.1 percent, to \$687.1 million. The entire balance of net assets in this fund is restricted for paying unemployment benefits by state and federal law.

Water Loan Programs

The net assets of the Water Loan Programs increased \$34.2 million or 6.1 percent from the prior year. Additional capital for loans was provided from \$14.4 million in dedicated sales tax revenues and \$13.4 million in federal grants, in addition to net operating revenues in the fund. Loans receivable for the programs increased \$24.4 million or 5.1 percent over the prior year. Of total net assets of \$597.9 million, \$236.2 million is restricted for use within the Water Loan Programs by bond covenants or by federal grant requirements.

CAPITAL ASSET AND LONG-TERM DEBT ADMINISTRATION

Capital Assets

The State's capital assets increased a net \$391.4 million during the year. The change consisted of net increases in infrastructure (highways) of \$155.9 million; land and related assets of \$56.9 million; and buildings, improvements, and construction in progress of \$181.1 million. Machinery and equipment decreased a net \$2.5 million during the year. Many buildings financed by the State are actually owned by the colleges and universities, which are discrete component units of the State. Therefore, while the capital assets are on the component unit's financial statements, any outstanding debt issued by the State to finance construction of those assets is reported as a liability of the State's governmental activities. This in turn reduces unrestricted net assets. As of June 30, 2006, the State had \$31.9 million of outstanding debt related to capital assets of component units.

At June 30, 2006, the State had \$226.2 million in commitments for building projects in its capital projects funds, and \$516.5 million (\$321.6 million in the Transportation Investment Fund and \$194.9 million in the Transportation Fund) in commitments for highway construction and improvement projects. Funding for the commitments will come from existing resources in these funds and from future bond proceeds and appropriations.

The State has adopted an allowable alternative to reporting depreciation for roads and bridges (infrastructure assets) maintained by the Utah Department of Transportation (UDOT). Under this alternative method, referred to as the "modified approach," UDOT must maintain an asset management system and demonstrate that the infrastructure is being preserved at or above established condition levels. Infrastructure assets accounted for under the modified approach are not depreciated, and maintenance and preservation costs are expensed.

The State's established condition level for roads is to maintain 50 percent with a rating of "fair" or better and no more than 15

percent with a "very poor" rating. The most recent condition assessment, completed for calendar year 2005, indicated that 69.5 percent of the roads were in "fair" or better condition. Only 6.3 percent of the roads assessed were in "very poor" condition. These results reflect a slight decline from conditions in calendar year 2004, when 74.7 percent of the roads were assessed as "fair" or better, and 6.2 percent assessed were in "very poor" condition.

The State's established condition level for bridges is to maintain 50 percent with a rating of "good" and no more than 15 percent of bridges with a "poor" rating. The most recent condition assessment, completed in April 2006, indicated that 71.0 percent and 2.0 percent of bridges were in "good" and "poor" condition, respectively. These results are similar to the prior year.

During fiscal year 2006, the State spent \$431.3 million to maintain and preserve roads and bridges. This amount is 52.2 percent above the estimated amount of \$283.4 million needed to maintain these assets at established condition levels.

More information about capital assets is included in Note 8 on page 82, and more detailed information on the State's modified approach for reporting infrastructure is presented in the Required Supplementary Information on page 114.

Long-term Debt

The *Constitution of Utah* authorizes general obligation borrowing only as approved by the Legislature. The *Constitution* also limits outstanding state general obligation debt to 1.5 percent of the fair market value of all taxable property in the State, while state law further restricts outstanding state general obligation debt to no more than 45 percent of the appropriations limit. As of June 30, 2006, the State was \$385.9 million below the statutory debt limit and \$1.548 billion below the debt limit established in the *Constitution*. Revenue bonds are not backed by the general taxing authority of the State, but are payable solely from specific fees or loan repayments as pledged in the bond indentures.

State of Utah
Net Outstanding Bonded Debt as of June 30
(Expressed in Millions)

	Governmental Activities		Business-type Activities		Total Primary Government		Total Percentage Change
	2006	2005	2006	2005	2006	2005	2005 to 2006
General Obligation Bonds	\$ 1,436.8	\$ 1,587.8	\$ —	\$ —	\$ 1,436.8	\$ 1,587.8	(9.5)%
Revenue Bonds:							
State Building Ownership Auth.	295.6	311.6	38.3	31.2	333.9	342.8	(2.6)
Student Assistance Programs	—	—	2,138.1	1,544.8	2,138.1	1,544.8	38.4
Total Bonds Payable	\$ 1,732.4	\$ 1,899.4	\$ 2,176.4	\$ 1,576.0	\$ 3,908.8	\$ 3,475.4	12.5 %

The State issued no new general obligation bonds during fiscal year 2006. The State issued a total of \$642.0 million of revenue bonds. Of the revenue bonds issued, \$8.4 million was to provide for capital facility construction, and \$633.7 million was to provide capital for purchasing student loans in the Student Assistance Programs.

The State's active management of its resources has helped the State maintain its triple-A rating on general obligation bonds, the highest possible rating, and double-A rating on State Building Ownership Authority lease revenue bonds from all three national rating agencies. These ratings save millions of dollars in interest each year because the State is able to obtain very favorable interest rates on new debt. Note 10 beginning on page 86 contains more information about the State's outstanding debt.

ECONOMIC OUTLOOK AND NEXT YEAR'S BUDGET

Tax revenues are expected to increase moderately in fiscal year 2007. However, original general revenue estimates for the General Fund and Uniform School Fund for fiscal year 2007 are slightly lower than actual fiscal year 2006 revenues. This is because actual fiscal year 2006 revenues were much stronger than anticipated, creating record surpluses. The Legislature balanced the 2007 budget primarily by using anticipated 2006 carryover funds of \$460.1 million and utilizing other miscellaneous sources. The Legislature provided increased funding for Medicaid, roads and highways, public and higher education, and capital projects. The State also provided a 3.5 percent cost-of-living adjustment to all state employees. An additional 2.75 percent or 5.5 percent compensation for market comparability adjustments was also provided for certain classifications within the Department of Corrections and the Utah Highway Patrol (a division of the Department of Public Safety).

Revenue collections to date in fiscal year 2007 are in line with original estimates.

Utah's economy is expected to remain stable in the near future. The average unemployment rate is expected to decline in 2006 to 3.3 percent, down from the average 2005 rate of 4.3 percent. Taxable retail sales are expected to increase 10.0 percent by the end of 2006, and growth in personal income is expected to be 9.0 percent for the same period. Because these indicators are measured on a calendar-year basis, the impact on the State budget will not be fully realized until well into fiscal year 2007.

CONTACTING THE STATE'S DIVISION OF FINANCE

This financial report is designed to provide our citizens, taxpayers, customers, investors, and creditors with a general overview of the State's finances and to demonstrate the State's accountability for the money it receives. If you have questions about this report or need additional financial information, please contact the Division of Finance, Financial Reporting Section at (801) 538-3082 or visit our Web site at: www.finance.utah.gov.

The preceding discussion and analysis focuses on the State's primary government operations. With the exception of a few nonmajor component units, the State's component units each issue separate audited financial statements that include their respective management's discussion and analysis. Component unit statements may be obtained from their respective administrative offices or from the Utah State Auditor's Office, Utah State Capitol Complex, East Office Building, Suite E310, Salt Lake City, UT 84114.

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